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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

NO. 77-454

MOORMAN MANUFACTURING COMPANY

Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA,

Appellee.

On Appeal From The Supreme Court
Of The State of Iowa

BRIEF FOR THE APPELLEE

RICHARD C. TURNER
Attorney General of Iowa

HARRY M. GRIGER
Assistant Attorney General
Lucas State Office Building
Des Moines, Iowa 50319

Attorneys for Appellee

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BRIEF FOR APPELLEE

OPINIONS BELOW

The Findings of Fact and Conclusions of Law of the Polk County District Court, Equity No. CE 3-1595, filed December 17, 1976, that Court's Ruling on Joint Motion to Reconsider and Supplemental Findings, and that Court's Judgment and Decree are unreported (A. 56). The decision of the Iowa Supreme Court, entered May 25, 1977, is reported at 254 N.W.2d 737 (Iowa 1977). That opinion and the unreported order denying rehearing entered June 27, 1977 are in the Appendix (A. 103,157).

JURISDICTION

Moorman invokes the jurisdiction of this court under 28 U.S.C. § 1257(2) since the Iowa Supreme Court held that the Iowa net income tax apportionment formula contained in § 422.33(1)(b), Code of Iowa, 1975, for reasonably attributing to Iowa a portion of Moorman's net income derived from the manufacture or sale of tangible personal property by the ratio which gross sales made within Iowa bear to total gross sales, did not, on its face or as applied to Moorman's net income, violate the commerce clause and the due process and equal protection clauses of the fourteenth amendment to the United States Constitution. The jurisdictional statement was filed September 22, 1977 and the Motion to Dismiss was filed October 20, 1977. Probable jurisdiction was noted November 14, 1977, 46 U.S.L. Week 3317 (U.S. Nov. 14, 1977), to review this decision of the Iowa Supreme Court.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Art. I, Sec. 8, Cl. 3 of the Constitution of the United States and the Due Process and Equal Protection Clauses of the Fourteenth Amendment thereto are set forth in Appendix A,p.Al, infra.

The relevant sections of the Code of Iowa, being Sections 422.33 and 422.35, Code of Iowa, 1975, contained in Volume II pages 1924 and 1925, are set forth verbatim in Appendix B, pp.A1-A4.

QUESTIONS PRESENTED

Whether the single-factor destination sales formula for the apportionment of net income prescribed by the Iowa income tax statute:

(1) discriminates against interstate commerce through the device of multiple taxation;

(2) subjects to Iowa tax a corporation's income out of all reasonable proportion to the business transacted in Iowa;

(3) constitutes the extraterritorial taxation of income; and

(4) subsidizes exports and imposes a tariff on imports;

in violation of the Commerce clause and the Fourteenth Amendment's Due Process and Equal Protection clauses of the United States Constitution.

STATEMENT OF THE CASE

This case was presented to the Courts below upon a stipulation of facts (A. 20-55). The only question on appeal to this Court concerns the constitutionality of the Iowa single sales factor net income apportionment formula.

Moorman, an Illinois Corporation, was engaged, during its fiscal tax years in question, March 31, 1968 through March 31, 1972, in the business of manufacture and sale of animal feeds. Such feeds were manufactured by Moorman in five plants located in Texas, Nebraska, and Illinois and sold by Moorman salesmen in more than 30 states. During the aforementioned fiscal years, Moorman carried on substantial income producing activities in the state of Iowa. After sales of feeds were negotiated by Moorman's Iowa sales force of over 500 employees, delivery to Iowa customers was typically made from one of six warehouses operated by Moorman in Iowa. Moorman engaged in no manufacturing in Iowa and the products sold to Iowa customers were all manufactured in Illinois. For the years in question, Moorman filed Iowa income tax returns, apportioning income to Iowa upon the basis of a three factor formula,

consisting of sales, property, and payroll factors, computed by it. For the years in question, the Iowa Director of Revenue (Director) recomputed Moorman's Iowa apportionable net income by application of the Iowa sales factor formula, rather than the three factor formula computed by Moorman. After notice and opportunity for hearing, the tax assessments which are the subject of this appeal were confirmed by the Director (A. 2-8). Moorman appealed the Director's determination to the Polk County District Court. The constitutional issues presented to the District Court were stipulated (A. 29-31).

The District Court held that the Iowa sales formula, on its face, violated the Commerce and Due Process, but not Equal Protection, clauses of the United States Constitution (A. 88). In reaching these conclusions, the District Court stated that "no evidence beyond that in the stipulation was presented or is considered" (A. 57). The only evidence in the stipulation upon which the District Court predicated its factual findings causing it to conclude that the Iowa formula was facially unconstitutional consisted of a showing that a three factor formula as computed by Moorman would result in a lower percentage of net income apportionable to Iowa than would the Iowa single sales factor (A. 75-76, 83-84). This evidence, together with the District Court's unfounded assumption that Iowa taxed 100% of Moorman's net income from Iowa sales, caused the Court to conclude that, based upon the interplay of the Iowa and Illinois apportionment formulae only, the percentage of Moorman's 1968 net income actually taxed was 141.76% and similar conclusions were reached for the other tax years (A. 84). The District Court was of the view that the constitutionality of the Iowa apportionment formula could be analyzed solely in terms of abstract computations of a three factor formula and Iowa single factor formula (A. 75-76, 83-84). The District Court assumed that an apportionment formula is facially unconstitutional if it does not provide for geographical distribution of labor and capital, thus reading into the Constitution a preference for an equally weighted three factor property-sales-payroll formula to the exclusion of other formulae (A. 75-77). The nature of Moorman's unitary income producing activities in all states, the profitability of its operations in all states, the precise jurisdictional sources of Moorman's net income in all states, and Moorman's net income tax base computations in all states were simply never considered by the District Court in making its findings and conclusions. Prior constitutional apportionment precedents, with their appropriate constitutional principles, were deemed insignificant by the District Court (A. 85). The District Court based its facial unconstitutionality holding upon *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965), despite the fact this Court expressly noted that such case was not decided on constitutional grounds (A. 77,85).

An additional Commerce Clause violation was found by the District Court based upon a hypothetical situation which assumed that the interplay between the Iowa and Illinois apportionment formulae gave the Iowa-based manufacturer a commercial advantage (A. 86). Such a finding was inconsistent with the District Court's initial statement to only consider the evidence in the stipulation (A. 57). As noted, infra, hypotheticals form no grounds for resolution of constitutional questions. Moreover, the conclusion here was inconsistent with the District Court's own determination that the equality of treatment of Iowa and non-Iowa corporations explained why the Iowa tax law was not in violation of the Equal Protection clause. (A. 72).

The Director appealed the District Court's decision to the Iowa Supreme Court, and Moorman cross-appealed. The Iowa Supreme Court unanimously reversed the District Court and held that the Iowa formula was facially constitutional and, further, that the formula was constitutional as applied to Moorman (A. 103-141). Unlike the District Court, the Iowa

Supreme Court noted that, for Due Process analysis, this Court's constitutional apportionment decisions recognize: (1) impossibility of achieving precise apportionment; (2) rough approximation is sufficient; (3) taxpayer's heavy burden in challenging apportionment formulae on constitutional grounds; and (4) the states are unrestricted in choosing apportionment formulae and have great leeway in making such choices (A. 130). The Iowa Supreme Court noted that for the Iowa formula to be facially unconstitutional, it must fail to achieve constitutional standards "in every conceivable situation," but that this could not logically happen (A. 131). The Court distinguished *General Motors Corporation v. District of Columbia*, supra, as expressly decided on nonconstitutional grounds, thus offering no precedent or support for facial invalidity of the Iowa sales formula (A. 125-130). The Court noted that Moorman's evidence merely showed a larger percentage of total net income apportioned to Iowa by the Iowa single factor formula than by Moorman's computed three factor formula, but that such evidence formed no basis to infer "either double taxation or a taxation of extraterritorial values" in violation of Due Process (A. 131-132).

The Due Process analysis along with the "potentially large deductions" in computation of the Iowa tax base were advanced as reasons by the Court for concluding that the Iowa formula did not facially violate the Commerce clause, the Court stating: "Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales" (A. 134). In essence, the Iowa Supreme Court concluded that the so-called "findings of fact" of the District Court were unjustified inferences, unsupported by the evidence, and were based upon unproven assumptions and improper analysis of the constitutional principles involved (A. 132,134).

The Iowa Supreme Court also determined that the Iowa sales formula did not facially violate Equal Protection, pointing

out that no evidence was introduced on this issue by Moorman which only attempted to show "extreme" hypothetical situations (A. 137). Thus, it was not shown, for Equal Protection purposes, that the Iowa sales formula subsidizes exports and imposes a tariff on imports.

The Court determined that the tenor of Moorman's contentions that the Iowa sales formula was unconstitutionally applied to its net income, as ordered by the Director, was inseparable from its allegations as to facial constitutionality (A. 138). Thus, having concluded the Iowa formula was facially valid, the Court held that Moorman had not carried its burden of showing that the Iowa formula was unconstitutionally applied to it (A. 138-139).

SUMMARY OF ARGUMENT

1. Prior constitutional precedents of this Court support the facial due process constitutionality of the Iowa statutory single sales factor net income apportionment formula. No showing has been made in this case that this presumptively valid formula produces, inherently, extraterritorial taxation or an income apportionment out of all reasonable proportion to corporate business transacted in Iowa. No such showing can be made by hypotheticals and assumptions as to the amount of income from Iowa sales taxed by Iowa.

2. The premise that the Iowa single sales factor formula operates to tax 100% of income derived from Iowa sales is unproven and false. Since this premise cannot be accepted, no showing was made that the Iowa sales formula facially causes multiple taxation and discriminates against interstate commerce in violation of the commerce clause. The abstract and hpothetical interplay of the Iowa formula and Illinois three factor formula is insufficient to demonstrate that the purpose and effect of the Iowa sales factor is to subsidize exports and

impose a tariff on imports. Moreover, precision in taxation is not required and if a formula produces rough approximation, it does not discriminate against interstate commerce.

3. All corporations doing business in Iowa and subject to Iowa income taxes are facially treated alike by the Iowa income tax scheme. Extreme hypotheticals are not proper tactics to demonstrate the facial invalidity of an apportionment formula under equal protection.

4. The tenor of Moorman's contentions as to facial constitutionality of the Iowa sales formula cannot be separated from its argument that the formula is invalid as applied to Moorman's net income. Nor was such a sufficient showing of invalidity presented. Therefore the Iowa formula is valid as applied to Moorman's net income.

5. Reversal of the decision of the Iowa Supreme Court would make the Constitution a formulary and inhibit the States, unduly, in the exercise of their fundamental power of taxation.

ARGUMENT

I. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate Due Process As Guaranteed By The Fourteenth Amendment To The United States Constitution.

The Iowa sales factor formula is contained in section 422.33(1), Code of Iowa and is a part of a statute regularly enacted by the Iowa legislature. As such, a review of the facial constitutionality of such statute requires this Court -- or any other Court -- to presume that the Iowa formula is valid. Both the trial court and the Iowa Supreme Court recognized this fundamental proposition and its corollary principles (A. 65-66, 115).

Moreover, as the Iowa Supreme Court pointed out, a facial constitutional attack upon a statute requires a showing by the challenger that the statute is unconstitutional "in every conceivable situation which might possibly arise" (A. 131). An examination of the Iowa sales formula contained in section 422.33(1), Code of Iowa, clearly discloses that it is not limited, in application, to non-Iowa manufacturers, like Moorman, but applies to any corporation carrying on its trade or business partly within and partly without Iowa and deriving income from the manufacture or sale of tangible personal property. Hence, the sales formula must be utilized by, among others, corporations manufacturing wholly in Iowa, manufacturing wholly outside of Iowa, manufacturing in Iowa and out of Iowa, and retail and wholesale merchants doing business within and without Iowa. In order for the Iowa sales formula to be facially unconstitutional, it must deprive all such corporate taxpayers of due process of law, and a mere possibility that some of them might be able to show such deprivation is not sufficient. Not all corporations doing business in Iowa are attacking the facial constitutionality of the Iowa formula. Indeed, the amicus brief of the Iowa Manufacturers Association clearly is evidence that there are corporate taxpayers who do not view the Iowa formula as violating their constitutional rights. Thus, Moorman can not, as a matter of law, make an appropriate constitutional attack upon the facial validity of the Iowa formula. Moorman cannot even show concretely that all corporations manufacturing wholly out of Iowa have been deprived of their constitutional rights by the Iowa formula.

The explanation of how the Iowa corporate net income tax operates is dealt with in the Iowa Supreme Court's opinion and is not really controverted by the parties herein (A. 105-106, 116-117). Section 422.33, Code of Iowa imposes the tax upon the net income of Iowa corporations and all foreign corporations "doing business in this state." Hence, the statute, by its terms, requires an income producing nexus in Iowa as a

prerequisite for imposition of the tax. No tax is imposed upon those corporations who merely ship goods into Iowa, but have no nexus here, such as the situation in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967). Those corporations engaged in a trade or business carried on partly within and partly without Iowa first compute net income derived from interest, dividends, rents, and royalties, and deduct such net income from their overall federal taxable income, as defined in section 422.35, Code of Iowa. The remainder of such net income, if derived from the manufacture or sale of tangible personal property within and without Iowa, is apportioned to Iowa by using the Iowa sales formula. Section 422.33(2), Code of Iowa, provides under the circumstances therein, for use of an alternative formula.

The basic test to determine whether a state tax violates due process guarantees is contained in *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 (1940):

> "The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society."

This basic due process test has also been incorporated into apportionment cases. *Norfolk & Western Railway Co. v. Missouri State Tax Commission*, 390 U.S. 317, 325, (1968) (footnote 5):

> " 'So far as due process is concerned the only question is whether the tax in practical operation has relation to

> opportunities, benefits, or protection conferred or afforded by the taxing state. See *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 [85 L Ed 267, 270, 61 S.Ct. 246, 130 ALR 1129]. Those requirements are satisfied if the tax is fairly apportioned to the commerce carried on within the State.' Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169, 174, 93 L.Ed. 585, 589, 69 S.Ct. 432 (1949)."

Consequently, unless Moorman can demonstrate that the Iowa sales formula does not fairly apportion its income to its activities in Iowa, no due process violation can occur. The stipulated evidence denotes that Moorman does business in Iowa and engages in extensive income producing activities in Iowa (A. 24-25). Its extensive use of salesmen in Iowa as well as its own warehouses allow it to exploit the Iowa market place. The State of Iowa allows corporations to do business, protects them in their business dealings, and provides for an orderly market in which Moorman and other corporations can transact business. The fact of the matter is that Moorman has sufficient contacts with the State of Iowa without which it could not sell approximately 20% of its products, for the years in question, in this state. Thus, for 1968 as an example, Moorman's Iowa activities produced $21,380,320 of gross Iowa sales (Exhibit 8, A. 36).

The foundational premise of the facial due process attack upon the Iowa sales formula by Moorman and its amici allies lies in their unproven assumption, adopted by the trial court but rejected as not true by the Iowa Supreme Court, that the Iowa sales formula taxes 100% of Moorman's net income derived from its Iowa sales of goods wholly manufactured in Illinois. Prior constitutional precedents of this Court conclusively demonstrate that such an unproven assumption does not satisfy a taxpayer's burden of overturning an apportionment formula on its face.

An analysis of prior constitutional apportionment precedents of this Court upholding single and multi-factor formulae will establish that these cases support the facial constitutionality of the Iowa sales formula in the instant case and do not support Moorman's appeal.

In *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920), this Court sustained the constitutionality of a Connecticut income tax statute which apportioned net income on the basis of a single property factor formula. This formula had the effect of apportioning 47% of a Connecticut based manufacturer's net income to Connecticut. An analysis of the evidence disclosed that the Iowa formula would have apportioned about 3.3% of such net income to the taxing state. (R. Item 3, p. 14). This Court stated at 254 U.S. 120-1:

> "The legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It therefore adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state."

This statement is completely apropos to Moorman in the instant case. This Court would not indulge in speculations and assumptions as to source of income or amount thereof but determined that the record did not disclose any concrete evidentiary showing by the taxpayer that the formula challenged was somehow improper. Contrary to Moorman's argument, this case does not support the assumptions made by Moorman. (Moorman Brief, pp. 30-31).

In *Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission*, 266 U.S. 271 (1924), a New York franchise tax measured by net income apportioned by a single assets factor, containing tangible and intangible property, was attacked upon due process and commerce clause grounds by a foreign-based manufacturer

whose only New York activity appeared to be a branch sales office located therein. It is quite possible that the use of the Iowa formula would have had the effect of apportioning no income to New York. (R. Item 3, p. 16). Economically, arguments could have been made, as Moorman repeatedly does, that the formula merely identified income, but did not apportion it, and that location of sales branch offices or the market place is irrelevant. However, the arguments would have been as invalid in that case as they are in the present case. This Court held that the constitutional questions were controlled "by the decision in *Underwood Typewriter Co. v. Chamberlain*." 266 U.S. 280. And, this Court stated at 266 U.S. 283:

> "There is no evidence in the record as to whether the company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain."

Note how this statement would preclude an assumption that the Iowa sales formula caused Moorman to be taxed on 100% of its income from its Iowa sales of goods manufactured in Illinois and would preclude the use of assumptions by Moorman to carry its burden of proof. (Moorman Brief, pp. 29-30).

Hans Rees' Sons, Inc. v. North Carolina, 283 U.S. 123 (1930) involved a constitutional attack, upon due process and commerce clause grounds, on the North Carolina single property factor formula as applied to the net income of a North Carolina based manufacturer. Unlike *Underwood* and *Bass*, the taxpayer introduced concrete evidence denoting that its income was derived from three sources, namely, buying profit, manufacturing profit, and selling profit. No speculation or conjecture was involved as to either the source or amount of such profits. This Court simply found that the evidence presented was competent to show that the single property factor formula

should not be applied to this particular taxpayer as it produced arbitrary and unreasonable results in the form of extraterritorial taxation. No such evidence has been offered in the instant case by Moorman. Whether Moorman's manufacturing activities produced a profit or a loss is unknown. It is not even known whether the net income actually taxed by Iowa contains any manufacturing profit at all.

In *Kent-Coffey Mfg. Co. v. Maxwell*, 291 U.S. 642 (1933), the North Carolina single property factor formula was again constitutionally attacked by a North Carolina based manufacturer. This formula apportioned 99.2% of taxpayer's net income to North Carolina whereas the Iowa sales factor would have apportioned .2% (R. Item 3, p. 18). The taxpayer relied upon *Hans Rees'* but such reliance, in view of the lack of an evidentiary showing, was held to be misplaced and the decision that the single property factor formula was constitutionally applied was based upon *Underwood*. Neither the North Carolina Court nor the United States Supreme Court would indulge in the assumption that the formula's effect upon Hans Rees' income would likewise be the same for Kent-Coffey's income, in view of Kent-Coffey's failure to introduce concrete evidence to overturn the formula. The decision in this case clearly refutes the tactics advocated by Moorman in its facial constitutional attack upon the Iowa sales formula.

Norfolk & Western Railway Co. v. North Carolina, 297 U.S. 682 (1936) involved the constitutionality of the North Carolina mileage formula to apportion net income of an interstate railway operating in and out of North Carolina. The railway introduced evidence concerning its operating expenses in North Carolina, but no evidence as to its actual and average gross revenues. This Court refused to speculate what such evidence might have shown. Once again, this Court was simply confronted with a state's apportionment scheme which was not shown by the taxpayer to be constitutionally infirm through

the evidence presented. Moorman's presentation rises to no higher level in the instant case. It should be noted that there is little difference between a mileage formula and a sales formula since a railroad's gross receipts it receives depends upon the mileage it generates. Such mileage has no necessary correlation to the amount of property and labor performed in the taxing state. This case supports the proposition that a sales formula is facially constitutional.

In *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939), this Court had for consideration the validity, upon due process and commerce clause grounds, of a Texas franchise tax in which the tax base was apportioned by a single gross receipts formula, as applied to the taxpayer, a motor vehicle manufacturer, doing no manufacturing activities in Texas. This Court sustained the tax, noting, contrary to Moorman's attempt (Moorman Brief, pp. 24-25) to distinguish it, that "It is much like that upheld in *Bass, Ratcliff & Gretton v. State Tax Commission.*" 308 U.S. 335. Indeed, this Court rejected the very rationale advanced by Moorman and its amici allies, namely, that an apportionment formula based upon geographical location of property is sound but one by sales is not, by expressly noting at 308 U.S. 336:

> "We reject petitioner's contention that constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula."

In *Butler Bros. v. McColgan*, 315 U.S. 501 (1942), this Court rejected a due process attack upon the California three factor (property, payroll, sales) formula as applied to the net income of a taxpayer, a merchant. This formula had the effect of apportioning 8.1372% of taxpayer's net income to California whereas the Iowa sales factor would appear to have apportioned 7.57% of such income to that state. (R. Item 3, p. 17). Citing the cases previously discussed herein, including *Ford Motor Co.*, this Court upheld the apportionment formula. This Court was

faced with a factual stipulation as the record evidence to decide whether the California formula was valid. This Court noted that the taxpayer had failed to show "the precise sources of its net income of $1,149,677." No assumptions, hypotheticals, or speculations were indulged in to overcome the presumption of constitutionality of the formula under attack. The taxpayer failed to show by clear and cogent evidence that the challenged formula was invalid.

In the aforementioned cases, taxpayers attacking the constitutionality of a statutory apportionment formula attempted to compare the results reached by the application of the challenged formula and some other method. In no case was such mere discrepancy of results reached between the challenged formula and some other method, per se, held to shift the burden to the state to justify its formula. In each case, this Court carefully inquired into the evidentiary record made in the courts below to determine whether sufficient evidence was presented to overturn the use of the challenged formula. In no case were assumptions and speculations by taxpayers as to source of income or amount allowed. Rather, the presumption was that the formula was valid until shown otherwise and all assumptions were indulged in to support the formula, not to defeat it. In no case were hypothetical examples entertained as satisfying the weighty burden of proof. Indeed, Hans Rees' won its case only by the actual evidence it presented. Clearly, Moorman's contentions and those of its amici attacking the Iowa sales formula can not be squared with the decisions of this Court in the aforementioned cases. Consequently, to presume that the Iowa formula taxes 100% of Moorman's income from its Iowa sales and that the Iowa formula apportions nothing simply would be inconsistent with this Court's decisions. We do not mean to suggest that the Iowa single sales factor formula can never be invalid as applied; only that it is not facially unconstitutional (and not unconstitutional as applied to Moorman's net income). For to hold that the Iowa formula is facially

invalid, as Moorman and its amici suggest, is to indulge in abstractions which this Court has declined to speculate upon. "We cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense." *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 463 (1959). In a number of the aforementioned cases, the amount of net income attributed to the taxing state by the apportionment formula sustained by this Court was greater than would have been the amount so apportioned by the Iowa single sales factor formula. That being the case, it can hardly be seriously contended that the Iowa sales formula is facially unconstitutional. There is no reason to suggest that the instant appeal should be treated differently than its constitutional predecessors by this Court.

Because of the complex nature of interstate business and the resultant inability to segregate the net income base of such business upon a geographical basis, the use of an apportionment formula is mandatory. And given this premise, this Court has never imposed upon the states a uniform apportionment formula, but has allowed the states great leeway in their choice of such formulae. Naturally, not all states will, therefore, adopt the same formula. And, because of the very nature of the undertaking, the formula used need only produce rough approximation, and not precision or even the best possible result. Indeed, as this Court pointed out in *International Harvester Co. v. Evatt*, 329 U.S. 416, 422 (1947):

> "Furthermore, this Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as those of appellant, and has declared that 'rough approximation rather than precision' is sufficient . . . unless a palpably disproportionate result comes from an apportionment . . . this Court has not been willing to nullify honest state efforts to make apportionments."

Therefore, in order to muster a constitutional attack upon a state's apportionment formula, the affected taxpayer has been given a very heavy burden of showing by clear and cogent evidence that the formula is invalid in the concrete factual circumstances which the taxpayer is required to present. *Butler Bros. v. McColgan*, supra; *Norfolk & Western Railway Co. v. North Carolina*, supra.

The aforementioned cases discussed herein contain the constitutional principles followed by the Iowa Supreme Court in analyzing Moorman's due process contentions and the Iowa Court's resolution and rejection of Moorman's arguments is analytically sound (A. 116-132).

On its face, the Iowa sales formula apportions net income to Iowa on the basis of an interstate corporation's business transacted in the Iowa market place – an obvious income producing activity. "The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut, and ending with sale in other states." *Underwood*, supra, at 254 U.S. 120. To argue, as does Moorman, that the Iowa sales factor merely identifies income but does not apportion it is not based upon any constitutional mandate, but is a mere economic theory. This argument is inconsistent with *Underwood* and *Ford Motor Co.*, in particular. In addition, to judically approve such an argument is to place an economic rigidity upon the interpretation of the Constitution by virtually requiring all states to adopt the three factor formula. As Justice Frankfurter stated:

> "We must be on guard against imprisoning the taxing power of the states within formulas that are not compelled by the Constitution but merely represent judicial generalizations exceeding the concrete circumstances which they profess to summarize." *Wisconsin v. J. C. Penney*, 311 U.S. at 445.

As noted, the Iowa sales formula is rationally related to due process requirements and is entitled to a presumption of constitutionality. A state, for example, Illinois, could have enacted a statutory single sales factor, a two factor (sales and property), or a three factor (sales, property, and payroll) formula, to apportion interstate net income. Indeed, Illinois has enacted a three factor formula. Such multi-factor formulae also, on their face, contain income producing factors and, are, thus, entitled to the presumption of constitutionality. Because there is no way, ordinarily, to specifically allocate the profits of a unitary multistate business on a geographical basis, it cannot be assumed that an apportionment formula containing one or more income producing activities is facially unconstitutional, notwithstanding that the apportionment formulae adopted by different states differ either in the factors included or in the computation of included factors. Thus, insofar as Moorman is concerned, there is nothing in the instant case indicating that the Illinois three factor formula apportions more or less net income to Illinois than actually earned there or that the Iowa sales formula apportions more or less net income to Iowa than actually earned in Iowa. While, for due process analysis, it is proper in apportionment cases to engage in assumptions to sustain apportionment formulae, it has never been considered proper to strike down such formulae on the basis of assumptions. Consequently, the cornerstone of Moorman's due process argument, to wit, the Iowa sales formula taxes 100% of Moorman's income from its Iowa sales, being a mere unproven assumption, cannot be and should not be accepted particularly in view of the heavy burden of proof Moorman has to show facial invalidity of an apportionment formula. Moreover, as the Iowa Supreme Court deftly pointed out, Moorman was not taxed upon 100% of such income (A. 134).

There is nothing in the record in this case which discloses that Moorman either proved that Iowa taxed 100% of its net income derived from Iowa sales, that the Director agreed with

such an assumption, or that the net income taxed was clearly derived from Illinois sources. Certainly, the figures contained on pages 12-13 and 27-28 of Moorman's Brief as well as the mathematical gymnastics in its Appendix E do not constitute such proof. Instead, for example, for the year 1968, the stipulated data discloses that Moorman had $97,719,800 of gross sales in all the states it did business in, of which $21,380,320 were attributed to the Iowa market place (Exhibit 8, A. 36). Thus, the record discloses at most that 100% of Moorman's gross income from Iowa sales was, for 1968, $21,380,320. But, Iowa did not levy its income tax upon this figure -- the only record evidence of income from Iowa sales. Rather, after allowance of deductions and application of the Iowa sales factor to Moorman's overall net income as defined in section 422.35, Code of Iowa, Iowa levies its tax upon $1,546,284 of Moorman's net income (Exhibit 8, A. 34). Obviously, the actual income taxed is not 100% of Moorman's income from Iowa sales, but merely a very small fraction thereof. To say, therefore, that Iowa taxed 100% of Moorman's net income from Iowa sales is to indulge in pure speculation -- and not very good speculation. There is nothing in the record of this case to show Illinois or any other state taxed any part of this $1,546,284. These same conclusions are applicable for Moorman's other tax years involved in this case.

The trial court agreed with Moorman that the Iowa formula taxed 100% of Moorman's net income from Iowa sales (A. 76-78). Moorman contends that the Iowa Supreme Court made no direct response to the findings of the trial court that the income which Iowa taxed was greatly attributable to Illinois plant and personnel inputs and was out of all reasonable proportion to business done in Iowa (Moorman's Brief, p. 22; A. 76, 77). As noted these findings are based upon the faulty premise that Iowa was taxing 100% of such income which the Iowa Supreme Court did respond to (A. 134). Moreover, it is not known, on the record herein, how much of such income, if

any, is actually attributable to the manufacturing process in Illinois. At most, the record in this case, as the Director pointed out in his Motion to Dismiss, only disclosed that, for example, 1968, based upon the abstract interplay of the Iowa and Illinois apportionment formulae, Iowa taxed 21.88% of Moorman's computed net income under Iowa law and Illinois taxed 41.76% of income not considering Illinois sales (Motion to Dismiss, p. 14, footnote 13). In view of this Court's pronouncements that rough approximation produced by formula apportionment is sufficient, the Iowa formula would still be facially valid even if a very small, but not disproportionate share, of Moorman's income taxed by Iowa could be actually attributed to Illinois. Exact precision in taxation is not required.

That Moorman relies upon hypothetical situations to satisfy its burden of showing the facial unconstitutionality of the Iowa formula is clearly demonstrated by Moorman's statement contained in its Petition For Rehearing to the Iowa Supreme Court:

> "Furthermore, facial unconstitutionality must be proven by the use of hypotheticals as was done in *General Motors*, where the facial invalidity of a regulation was at issue. In no other way can a litigant negative every reasonable basis which may support the statute. In the case before this Court, Moorman has proven the facial unconstitutionality of § 422.33(1)(b) by the use of hypotheticals, none of which have been challenged." (A. 151).

If this statement by Moorman was a correct exposition of the constitutional standards involved in a due process attack upon an apportionment formula, there would be little or nothing to present in the way of an evidentiary attack upon such formula. All that would be necessary in apportionment cases is the production of an economist's brief – as, indeed, has been presented by Amici Baumol et al. Thus, the constitutionality of apportionment formulae would depend upon the acute and

powerful economic intellect, not upon the constitutional standards evolved by this Court in apportionment cases.

It is axiomatic that hypotheticals form no basis for constitutional attacks upon statutes. *United States v. Raines*, 362 U.S. 17 (1960). In particular, the use of hypotheticals has never been condoned by this Court to show the invalidity of apportionment formulae. The above quoted statement by Moorman is so obviously inconsistent with *Underwood Typewriter Co. v. Chamberlain*, supra; *Bass, Ratcliff & Gretton Ltd v. State Tax Commission*, supra; *National Leather Co. v. Massachusetts*, 277 U.S. 413 (1928); *Hans Rees' Sons, Inc. v. North Carolina*, supra; *Kent-Coffey Mfg. Co. v. Maxwell*, supra; *Norfolk & Western Railway Co. v. North Carolina*, supra; *Ford Motor Co. v. Beauchamp*, supra; *Butler Brothers v. McColgan*, supra; *International Harvestor Co. v. Evatt*, supra. This statement is clearly inconsistent with this Court's refusal to deal with abstractions in *Northwestern States Portland cement Co. v. Minnesota*, supra, 358 U.S. 463. This statement, in essence, is an admission by Moorman that it cannot show by concrete facts that the Iowa formula is facially unconstitutional.[1]

Moorman states in its brief that the "only rationale for taxes is government services" (Moorman Brief, p. 17). The Director agrees. "The simple but controlling question is whether the state has given anything for which it can ask return." *Wisconsin v. J. C. Penney Co.*, supra, 311 U.S. 444. But, then Moorman contends that imposition of income taxes, to be consistent with the above rationale, must be quantitatively related to the property and employees of the taxpayer located in the taxing state and the location of the market place in which

1. The Court's attention is directed to the case quotes on pages 11-12 of the Director's Motion To Dismiss. The use of hypotheticals as an adequate showing of either facial unconstitutionality or unconstitutionality as applied cannot be squared with the quotations from these cases. The principles contained in these cases were followed in this case by the Iowa Supreme Court but ignored by the trial court.

sales are made is irrelevant. Not only does this point lack merit, but this Court in essence rejected it, for purposes of approving an unapportioned gross receipts tax in *Standard Pressed Steel Co. v. Washington*, 419 U.S. 560 (1975). While it is undisputed that Moorman has significant amounts of people and property in Iowa, even if Moorman had no property in Iowa and few salesmen, it would be a sufficient beneficiary of government services so as to be required to pay Iowa income tax on income it earned from the Iowa market place. Such a result would be no more onerous – and probably less – than this Court's decision in *Standard Pressed Steel Co.* Moorman's argument that an income tax is facially invalid unless an apportionment formula considers relative quantities of property and people is undermined by this Court's statement in *Ford Motor*, supra at 308 U.S. 336:

> "We reject petitioner's contention that constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula."

Moorman attempts to distinguish *Ford Motor* as well as other cases cited by the Iowa Supreme Court in support of the facial constitutionality of the Iowa sales formula. (Moorman Brief, pp. 24-25). Indeed, Moorman contends that *Underwood*, *Kent-Coffey*, and *Bass* support the trial court's decision.[2] In the gross receipts apportionment formula *Ford Motor* case, this Court relied upon its holding in *Bass*, sustaining a single assets factor formula. In *Bass*, this Court held that the constitutionality of the assets formula was controlled by the *Underwood* decision sustaining a single property factor. *Kent-Coffey* was wholly decided by this Court on the basis of *Underwood*. In the three factor case of *Butler Bros*, the *Ford Motor* case was cited with approval and as support for this Court's decision to sustain such formula.

2. The trial court felt such cases were of little significance and did not rely upon them (A. 85).

Therefore, regardless of the type of tax or formula involved, this Court has relied upon all such cases and has never sought to distinguish them. Also, *Underwood* which upheld an apportionment formula as applied to an instate manufacturer was used to control the decision in *Bass* relating to apportionment of income of a manufacturer doing no manufacturing in the taxing state. Consequently, it is clear that these cases support the conclusion of the Iowa Supreme Court that the Iowa sales formula is facially constitutional. Moorman's analysis of these cases that they support its appeal herein is clearly incorrect.

In its brief, Moorman, unlike its Jurisdictional Statement, purports to state that it now makes no demand upon this Court to prescribe any specific formula to apportion income (Moorman Brief, p. 31). A closer reading of this Brief discloses that Moorman considers a single property factor facially "sound" (Moorman Brief, p. 25) and, obviously, a three factor formula.[3] In this connection, Moorman concedes that such formulae, which could apportion more income to Iowa than under the Iowa taxing scheme, are facially valid, a self-defeating admission insofar as facial constitutionality is involved.[4] Clearly, the use of such formulae by Moorman would apportion less computed Iowa net income pursuant to Iowa Code section 422.35 than would the Iowa sales formula because of Moorman's factual situation. However, Moorman attacks the weighted 3 factor formulae (double weight on sales) of Florida, Wisconsin, New York, and Massachusetts. (Moorman Brief, p. 39). The stipulated data will disclose that such facially valid weighted three factor formulae applied to the Iowa net income base without a federal tax deduction would have apportioned $241,409 more

3. Both in its Jurisdictional Statement and in its Brief, Moorman claims to have used the three factor formula contained in the Uniform Division of Income for Tax Purposes Act. The Director commented upon this point in his Motion to Dismiss (Motion to Dismiss, p. 3, footnote 1).

4. See prior discussion in this brief on comparison of Iowa formula with formulae upheld in these cases.

net income of Moorman to Iowa than the Iowa tax scheme (Exhibit 8, A. 52). Consequently, Moorman purports to accept a single property factor formula and its three factor formula, but not much else. Thus, Moorman, in essence, is attempting to make the Constitution a strict formulary by "graciously" accepting the equally weighted three factor formula. Such a view is clearly inconsistent with any apportionment case ever decided by this Court and cannot be squared with the due process principles consistently formulated by this Court over many years and duly adhered to by the Iowa Supreme Court in this case (A. 130).

Moorman's evidence, which it claims the Director did not rebut, rose no higher than a showing that its computed three factor formula apportioned less net income from the sale of tangible personal property attributed to Iowa than would the Iowa sales formula. To this, the Iowa Supreme Court made appropriate response:

> "However, the mere fact application of the single factor formula results in a larger percentage being used for ascertaining the Iowa portion of the corporation's net income than would application of some other type of formula does not render the apportionment provision of the Iowa corporate income tax law facially unconstitutional in violation of due process clauses of the federal and state constitutions. Such evidence alone does not establish that the difference between the two figures represents either double taxation or a taxation of extraterritorial values. Fairness is not equated with absolute precision." (A. 131-132).

Under the constitutional principles which this Court has evolved and expounded in apportionment cases, the taxpayer seeking to invalidate an apportionment formula must come forward with clear and cogent evidence to negate the use of such formula. Once that occurs, the State must rebut such evidence or lose. *Norfolk & Western Railway Co. v. Missouri*

State Tax Commission, 390 U.S. 317 (1968). But, the State is not required to inform a taxpayer how to invalidate a statutory apportionment formula and until the taxpayer has come forward with such evidence, the State can merely stand on its formula. Nowhere is this more clearly demonstrated than in *Bass*, *Underwood*, *Ford Motor*, and *Butler Bros*, in which the State never presented evidence to rebut the showing made by the taxpayer. Indeed, the evidence produced by the taxpayer and not rebutted by the State in *Butler Bros* was far more extensive in concrete terms than Moorman presented. The mere fact that an evidentiary showing can be made to invalidate a single factor formula under concrete circumstances does not render the formula facially invalid under all conceivable circumstances. Nowhere is this point more clearly expressed than by the decision in *Underwood* upholding the single property factor, later decision in *Hans Rees'* invalidating the property formula as applied, and subsequent decision in *Kent-Coffey* upholding the property formula. The State is also not required to rebut assumptions and hypotheticals contrived by Moorman and its amici (although we have pointed out the underlying fallacies of them). The Director has, however, demonstrated herein that Moorman was not taxed upon 100% of its income from Iowa sales -- a factual conclusion adopted by the Iowa Supreme Court (A. 134).

Moorman contends that the Iowa sales factor subsidizes exports and imposes a tariff upon imports in violation of due process. (Moorman Brief, p. 8). The same contention is made to assert that the Iowa formula violates the commerce clause. (Moorman Brief, p. 15). The Director believes that such a contention is addressed to a question of discrimination against interstate commerce. In any event, the Director will deal with this issue in the commerce clause portion of his brief, incorporating herein by reference his discussion thereof.

The Iowa Supreme Court found that the Iowa "formula in

question meets the due process requirement of attempting to fairly allocate the corporation's income" (A. 132). It is respectfully submitted that the Iowa Court's decision that the Iowa formula is not facially violative of due process is amply supported by reason and law and should be sustained by this Court. No showing has been made that the Iowa formula, on its face, caused or produced extraterritorial taxation or subjected to Iowa tax Moorman's income out of all reasonable proportion to Moorman's business transacted in Iowa.[5]

II. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate the Commerce Clause of the United States Constitution.

The Iowa Supreme Court noted:

> "The considerations applicable to the resolution of a due process challenge to an apportionment formula are substantially similar to those utilized in assessing the validity of that formula with respect to the commerce clause. Extraterritorial taxation is constitutionally defective 'both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.' Norfolk & W.Ry. Co. v. Missouri State Tax Com'n, supra, 390 U.S. at 325, 88 S.Ct. at 1001, 19 L.Ed.2d at _____." (A. 132).

It is a violation of the commerce clause (Article I, Section 8, Clause 3) of the United States Constitution to subject interstate commerce to the risk of multiple state taxation and to discriminate against interstate commerce in favor of locally based industry through state taxation. *Standard Pressed Steel Co. v. Washington*, supra; *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977).

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5. In addition to Due Process, Moorman argued the Iowa formula violated a fundamental principle of federalism. This issue has never been raised in any previous stage of these proceedings. It also has no merit.

Like the arguments made for due process violation, the foundation of Moorman and its allied amici's contentions that the Iowa sales formula facially violates the commerce clause rests upon the hypothesis that the Iowa formula taxes 100% of the income derived from Iowa sales of goods manufactured in Illinois. The Director's analysis and rebuttal of this premise in the due process portion of his brief are also incorporated herein by reference. And, such an unproven hypothesis cannot satisfy Moorman's weighty burden of showing by clear and cogent evidence that the Iowa formula is facially invalid. Multiple taxation, in the constitutional sense, is not shown merely because the Iowa apportionment formula does not guarantee precision. As long as roughly approximate results exist, this Court has not striken an apportionment formula upon commerce clause grounds.

The presence of multiple state taxation of Moorman's net income cannot rest upon an abstract assumption that Iowa taxed or risked the taxation of 100% of income derived from Moorman's Iowa sales and cannot rest upon the abstract interplay between the Iowa and Illinois apportionment formulae (Moorman Brief, pp 10-13). Indeed, as this Court stated in *Northwestern States Portland Cement Company v. Minnesota*, 358 U.S. 450, 463:

> "There is nothing to show that multiple taxation is present. We cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense. This they have failed to do."

Likewise, Moorman has failed to demonstrate that multiple taxation is present in this case.

The amicus brief of the multistate tax commission and attorney general of the State of Oregon indicates that states, other than Iowa, have constitutionally exerted their taxing

power over corporations with unitary subsidiaries by including in the net income base subject to formula apportionment the entire business net incomes of the parent and subsidiary corporations (Commission Brief, p. 5). The Director did not require Moorman to file an Iowa consolidated return and did not apportion to Iowa any of the net income of Moorman's subsidiaries (A. 23). Thus, Moorman has not demonstrated in this case that all of its unitary apportionable net income was subjected to taxation by Iowa to the extent other states so tax or can tax Moorman. That being the case, there should be no inference of overlapping state taxation of Moorman's unitary income because of the Iowa formula.

Moorman contends that the tax base is irrelevant to considerations of multiple state taxation involving an apportionment formula (Moorman Brief, pp. 13-15). Yet, the tax base can be relevant to disclose that a state has not exceeded the full extent of its constitutional authority in the practical operation of the tax. In *Standard Pressed Steel Co. v. Department of Revenue*, supra, this Court considered the constitutionality of the Washington business and occupation tax levied upon the unapportioned gross receipts derived by the taxpayer from interstate sales to a customer located in Washington. An employee of the taxpayer was constantly in Washington, but did not take any sales orders from the Washington customer who sent such orders outside of Washington for acceptance by the taxpayer. This Court sustained the levy of the tax on the taxpayer's gross income from such interstate sales on the basis of *General Motors Corp. v. Washington*, 377 U.S. 436 (1964). This Court rejected the taxpayer's contention that a risk of multiple taxation was demonstrated at 419 U.S. 563:

> "We noted in General Motors that a vice in a tax on gross receipts of a corporation doing an interstate business is the risk of multiple taxation; but that the burden is on the taxpayer to demonstrate it, id., at 449, 12 L.Ed 2d 430. The corporation made no such showing there. Nor is any

effort made to establish it here."

In the instant case, to repeat, the stipulated data discloses that Moorman made Iowa sales in 1968 of $21,380,320 (Exhibit 8, A. 36). Under *Standard Pressed Steel*, Iowa could have taxed this amount without risking double taxation, but instead, for that year, Iowa taxed $1,546,284. Moorman has made no showing where this $1,546,284 was actually earned. But, at most, it inferentially represents a mere fraction of the $21,380,320 and it obviously cannot be considered to represent 100% of the income derived from Iowa sales by Moorman. Consequently, the Iowa Supreme Court correctly concluded that Iowa did not tax 100% of Moorman's income from Iowa sales in view of the Iowa tax base. If Iowa, in 1968, could have levied an unapportioned gross income tax upon Moorman and other corporations similarly situated why cannot Iowa levy its tax upon a lesser apportioned net amount?

Moorman makes an irrelevant argument to the effect that the reason why the tax base is irrelevant is because a high tax base produces a low tax rate and a low tax base produces a high tax rate (Moorman Brief, p. 14). The wisdom of having a high or low tax base or tax rate is not of concern here. "The wisdom of state net income taxes is one of state policy not for our decision." *Northwestern States Portland Cement Company v. Minnesota*, 358 U.S. 462.

As noted in the due process portion of this brief, Moorman has never demonstrated, concretely, that the Iowa sales formula caused extraterritorial taxation to be visited upon Moorman or any other corporation. In view of assumptions and presumptions used in apportionment cases, it must be assumed that the Iowa formula would reach profits reasonably attributable to Iowa. Logically, therefore, there is no basis for concluding that the Iowa formula causes actual or a risk of multiple taxation because of enactment of this formula by the Iowa legislature. Moorman's posi-

tion is that the Iowa formula, regardless of the facts, inherently taxes profits earned outside of Iowa, without proof such is the case, in every conceivable situation imagined. This position is obviously inconsistent with this Court's constitutional apportionment case precedents and principles therein, in some of which more income was actually apportioned to the taxing state than would have been by using the Iowa formula. No multiple taxation or discrimination against interstate commerce was found in those cases. The mere possibility that there may be come multiple state taxation affecting particular taxpayers at various times under some conceivable circumstances would not show the Iowa formula facially invalid.

Moorman contends that the Iowa sales formula subsidizes exports and imposes a tariff on imports, thereby discriminating against non-Iowa based manufacturers by granting Iowa based manufacturers a competitive advantage because non-Iowa based manufacturers are subjected to multiple taxation (Moorman Brief, pp. 15-17). Like all of its other arguments, this argument of Moorman's concerning alleged discrimination against interstate commerce rests upon the faulty premise, refuted by the Iowa Supreme Court, that 100% of Moorman's income derived from its Iowa sales is apportioned to and taxed by Iowa. It is clear that, on its face, the Iowa income tax scheme is not discriminatory. Section 422.33, Code of Iowa, which imposes the tax, sets the tax rates, and provides for apportionment of interstate income, does not, on its face, provide different and discriminatory treatment for local corporations or foreign corporations similar to Moorman's situation. Section 422.35, Code of Iowa, which defines the tax base does not grant a different base to Iowa corporations and foreign corporations. Insofar as the Iowa apportionment formula is concerned, it applies to all corporations selling goods in the Iowa market place and earning income there. Hence, the Iowa taxing scheme, standing alone, does not constitute a discrimination against interstate commerce nor an unconstitutional risk of multiple

taxation. Since the formula applies to all interstate corporations doing business in Iowa apportioning only the portion of their income earned here and since Section 422.33, Code of Iowa, taxes 100% of a corporation's income earned wholly intrastate in Iowa, no facial discrimination against interstate commerce exists. Clearly, a reading of the Iowa net income tax statute in Section 422.33, Code of Iowa, will not disclose, facially, any practical discrimination against interstate commerce of any type.

Moorman, however, does not simply consider whether the Iowa formula, standing alone, creates a risk of multiple taxation and discrimination against interstate commerce. Moorman concludes the Iowa sales formula violates the commerce clause by granting Iowa based corporations competitive advantages on the basis of the abstract interplay between the Iowa sales formula in the context of other states', notably Illinois, use of the three factor formula. Again, of course, this contention indefensibly assumes that Iowa taxed 100% of the income derived from Iowa sales and assumes there must be overlapping taxation. This conclusion is wrong for the further reason that it allows the configuration of laws of other states, in the abstract, to dictate the constitutionality of the Iowa law. We know of no case where this Court has stricken, on commerce clause grounds, an apportionment formula or any tax scheme on such a basis.

Consider, for example, the situation if the only state which had enacted an income tax was Iowa. The Iowa sales formula would apportion income of all interstate corporations to Iowa. Next, Illinois decides to impose an income tax apportioned by a destination sales formula. No multiple taxation or discriminatory taxation would arise.[6] Then, all states impose income taxes

6. This is conceded in the Amicus Brief of the Council of State Chambers of Commerce (COST Brief, p. 8, footnote 7).

apportioned for interstate commerce by the destination sales factor. Again, no commerce clause problems. But, suppose one state, i.e. Illinois, decided to change its law and apportion income by a three factor formula. Under Moorman's theory of commerce clause violation, the Iowa sales factor now violates the Constitution because of the laws enacted by the State of Illinois or perhaps the Illinois law is invalid because it is so different from other state formulas. But, there was no multiple taxation or discrimination before Illinois adopted the three factor formula. Consequently, Illinois, not Iowa, under Moorman's argument carried to its logical conclusion, created a risk of multiple taxation. The Director is not saying herein that the Iowa sales formula or the Illinois three factor formula actually create a risk of multiple state taxation. The point is simply this: If the facial constitutionality of the Iowa sales formula concerning discrimination against interstate commerce is to be dictated by legislatively created tax formulae adopted in other states, then it would be impossible for the states to tax net income derived from interstate commerce except by the rigid exact adoption of the same tax scheme including formulae, base, and rates. Further, the first state to adopt an income tax and apportionment formula dictates to the other states to conform their tax schemes thereto or lose them through the device of discriminatory multiple taxation. The wide leeway this Court has afforded the states in their choice of apportionment formulae would disappear. While not a commerce clause precedent, this Court put it well in *Austin v. New Hampshire*, 420 U.S. 656, 668 (1975):

> "Nor, we may add, can the constitutionality of one state's statutes affecting nonresidents depend upon the present configuration of the statutes of another state."

Under Moorman's theory of this case, the Constitution would become the very formulary this Court held it was not in *Wisconsin v. J. C. Penney Co.*, supra, and the configuration of

statutes in other states would dictate the facial constitutionality of the Iowa sales formula, contrary to the above principle enunciated in *Austin*. Moorman's analysis that the Iowa sales formula imposes a tariff upon imports and subsidizes exports is unsound because the Iowa formula, standing alone, cannot have that effect. As long as Iowa properly exercised its taxing power, a commerce clause violation cannot depend upon how Illinois or any other state properly exercises its taxing powers.

The fact of the matter is that Moorman's complaint that it is subjected to different state apportionment formulae raises a political, not a constitutional, question. In this regard, it is not irrelevant to note that Congress, in which the commerce power is placed by the Constitution, has frequently addressed the question of providing for a uniform net income tax apportionment formula and each time has refused to impose upon the states the straightjacket demanded by those who are unable to find in the Constitution's commerce clause support for the exclusivity of the formulae they expouse. See, e.g. S. 1245, 93rd Cong. 1st Sess. (1973); H.R. 1538, 92nd Cong., 1st Sess. (1971); H.R. 669, 95th Cong. 1st Sess. (1977).

Moorman, in attacking the facial constitutionality of the Iowa formula, must negative every reasonable basis which might support the formula. Its attempt to do so by hypotheticals has never been considered by this Court as acceptable, but such tactics have been rejected. Therefore, its assertion that the Iowa formula subsidizes exports and imposes a tariff upon imports is unproven and must necessarily fail. There is no basis for a conclusion that the Iowa formula constitutes "protectionist" legislation for Iowa based manufacturers. It would be an extremely marginal situation to find an Iowa-based manufacturer not selling goods in the Iowa market place. Faced with the impossibility of specifically allocating an interstate corporation's net income on a geographical basis, the Iowa legislature could have concluded that all corporations doing business in

Iowa and exploiting the Iowa market place should apportion net income which they derive in all states they do business in on the basis of sales and that such an apportionment would be fair to Iowa-based and non-Iowa based corporations. Such a determination by the Iowa legislature is clearly consistent with the cases cited herein approving single and multi-factor formulae. It has not been rebutted by Moorman.

Moorman and its amici rely heavily upon this Court's decision in *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965). They claim that this case fully supports their contention that the Iowa formula is facially unconstitutional and that a showing of such unconstitutionality can be made by assuming that Iowa taxes 100% of the income Moorman derives from its Iowa sales and by demonstrating hypotheticals. These contentions should be examined in light of what this Court decided in *General Motors*, the statutory provisions involved, and what this Court did not decide. In that case, the taxpayer, a manufacturer of motor vehicles outside of the District of Columbia and a seller thereof in the District, challenged upon constitutional and statutory grounds a regulation promulgated by the District Commissioners to apportion net income to the District by a single sales factor formula. The Court of Appeals for the District of Columbia held that the regulation was consistent with the general statute providing for no specific formula but authorizing the Commissioners to promulgate one and that the regulation was constitutional (336 F.2d 885). This Court reversed that decision "without reaching the constitutional questions presented." 380 U.S.555. While critical of a single sales factor formula, this Court noted that it has never attempted to define one exclusive apportionment formula for the states to use. 380 U.S. 561. No position on the constitutionality of a single sales factor formula was taken – none at all. "We of course do not mean to take any position on the constitutionality of a state income tax based on the sales factor alone." 380 U.S. 561. Instead, this Court found that the District formula was unsup-

ported by the statute. Thus, what this Court was actually doing was determining that the formula adopted by the District was not consistent with the legislative intent of the District statute. That statute not only provided that the net income of multistate corporations must be fairly attributable to the trade and business engaged in the District, but required the Commissioners, in exercising their discretion in promulgating a regulation, to adopt an apportionment formula to include factors related to all portions of the corporation's business within and without the District. 380 U.S. 557. This point was correctly recognized by the Iowa Supreme Court in this case (A. 130). In *General Motors*, therefore, this Court was not faced with the question of the facial constitutionality of a statutory single sales factor formula and because the case was decided upon nonconstitutional grounds and, thus, merely involved the question of whether the exercise of administrative action was supported by the enabling statute, this Court could and did find it necessary to use hypotheticals and assumptions to depict how the single sales factor the Commissioners adopted simply did not do what the statute required, namely, to consider in the formula the fact that General Motors was engaged in manufacturing activities outside of the District, whether those activities actually produced any net income for General Motors or not. This Court declined to promulgate an apportionment formula for the Commissioners and left that action to them. 380 U.S. 562. This Court approved of single property factor formulae and a three factor property-payroll-sales formula. No finding by this Court was made that, in fact, the sales factor formula violated the principles embodied in the due process and commerce clauses.

The Court's decision in *General Motors* surely does not relieve a taxpayer challenging the constitutionality of the Iowa single sales factor formula of the very heavy burden to demonstrate beyond a reasonable doubt by clear and cogent evidence that the formula is invalid. The decision does not

sanction a showing of unconstitutionality upon the hypothesis that Iowa taxed 100% of Moorman's income derived from its Iowa sales when, in fact, there is no evidence of this and what evidence there is compels a contrary conclusion. Indeed, as the Court of Appeals pointed out, there was no unity of agreement among economists as to the rational impact of a sales factor or even as to the factors which should be part of an apportionment formula. 336 F. 2d 899. This is all the more reason for concluding Moorman has not shown the facial invalidity of the Iowa sales formula and for this Court not to facially condemn such formula. The constitutional principles expounded by this Court in prior constitutional precedents were not overruled in *General Motors*. Application of those principles, as the Iowa Supreme Court correctly observed, compel the conclusion that the Iowa sales formula is facially constitutional and no commerce clause violation has been demonstrated in this case.

III. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate Equal Protection As Guaranteed By the Fourteenth Amendment To The United States Constitution.

Once again, by the use of hypotheticals (and extreme ones at that), Moorman attempts to show constitutional transgression. (Moorman Brief, p. 33). No evidence is introduced on this constitutional issue of equal protection. In considering Moorman's facial equal protection attack upon the Iowa formula, all presumptions must be indulged in to support the validity of the formula and Moorman must negate all conceivable bases which support the statute. Quite clearly, Moorman has not done this, for as the Iowa Supreme Court noted:

> "Moorman's only attempt to demonstrate the unreasonableness of the classification contained in section 422.33(1)(b) is with reference to admittedly 'extreme' hypothetical situations. Such a tactic clearly does not establish the classification is unreasonable." (A. 137).

Moorman's equal protection argument is, in substance, no different than its due process and commerce clause contentions. The gist of this argument is that the abstract interplay of the Iowa sales formula with those three factor formulae used by other states provides benefits to Iowa businesses unavailable to Moorman. No evidence was introduced on this point. Indeed, Moorman did not even bother to point out its competitors who were the alleged recipients of such advantages, all caused by the Iowa sales formula. [7] It is inconceivable that a corporation with Iowa activities as extensive as Moorman receives less benefits than Iowa based corporations. All corporations doing business in Iowa are the recipients of an orderly market provided by Iowa and all corporations receive protection from Iowa in engaging in such Iowa business.

Historically, this Court has refused to declare acts of Congress or state legislatures unconstitutional on the basis of hypothetical cases. *United States v. Raines*, 362 U.S. 17; *New York v. O'Neil*, 359 U.S.1 (1959). Therefore, it would be entirely consistent with such cases for this Court to refuse to find a facial equal protection infirmity on the basis of the hypothetical argument presented by Moorman in this case.

In *Madden v. Kentucky*, 309 U.S. 83,88 (1940), this Court stated:

> "It has, because of this, been pointed out that in taxation, even more than in other fields, legislatures possess the greatest freedom in classification. Since the members of a legislature necessarily enjoy a familiarity with local conditions which this Court cannot have, the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislative arrangement to negative every conceivable basis which might support it."

Moorman has not satisfied its burden as disclosed in *Madden*.

No taxing scheme need be perfect to pass constitutional muster. In *San Antonio School District v. Rodriques*, 411 U.S. 1,41 (1973), this Court stated:

> "No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods and services, has yet been devised which is free of all discriminatory impact. In such a complex arena in which no perfect alternatives exist, the court does well not to impose too rigorous a standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection Clause."

Consequently even if a competitor of Moorman was based in Iowa, did all of its manufacturing here, and exported all of its goods out of Iowa, such a stituation would not facially invalidate the Iowa sales formula. To say that it would requires an iron rule of equal taxation to satisfy equal protection whereas no such iron rule has ever been required, but in fact rejected, by this Court.

On its face, Section 422.33, Code of Iowa classifies all corporations doing business in Iowa exactly alike with respect to calculation of tax base, apportionment formula, and rate of taxation. No class of foreign corporations manufacturing and selling tangible personal property is singled out for treatment different than any such corporations based in Iowa. Moorman, by its own admission, does not come within the extreme situations it hypothesizes in its Brief. Thus, the Iowa sales formula does not facially violate equal protection.

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7. There is nothing in the record in the present case to show that such companies, as listed by Moorman in its two hypothetical situations, are engaged in Iowa in such activities (Moorman Brief, p. 33).

IV. The Application Of The Iowa Statutory Sales Factor Formula To Moorman Is Not Unconstitutional.

Moorman contends that if the Iowa sales formula does not facially violate due process, commerce clause and equal protection, it is invalid as applied to Moorman. In this regard, Moorman essentially posits the same arguments which it made for facial constitutionality and relies upon the same stipulated data (Moorman Brief, p. 36). But, that data rises to no higher level than that Moorman's three factor formula would result in less net income, as computed under Section 422.35, apportioned to Iowa than would the use of the Iowa sales formula. That data does not show that Moorman was subjected to multiple taxation, discrimination, or extraterritorial taxation based upon the assumption that Moorman was taxed upon 100% of its income derived from its Iowa sales. The Iowa Supreme Court correctly found this assumption not to be the fact. The only evidence in the record denoting 100% of Moorman's income from Iowa sales consists of *gross* income which for 1968 as an example was $21,380,320 whereas the Iowa apportioned net income for 1968 only attributed $1,546,284 of Moorman's overall federal taxable income to Iowa (Exhibit 8, A. 34,36). For the other tax years in question, Moorman's net income subject to tax was always less than 100% of its income from Iowa sales (A. 34,36). The Iowa Supreme Court correctly concluded that Moorman could not possibly have been subjected to Iowa tax on 100% of its income from Iowa sales (A. 134). The Iowa Court correctly concluded:

> "No evidentiary justification is provided for a conclusion Moorman is somehow different from those corporations legitimately subject to the provisions of section 422.33(1)(b). In the absence of such evidence Moorman has not made out a sufficient case for overturning on constitutional grounds the application of the Iowa single-sales factor formula to its net income." (A. 139).

In *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*, supra, at 266 U.S. 283, this Court stated with reference to a manufacturing corporation in the same situation as Moorman:

> "There is no evidence in the record as to whether the company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain."

In *Norfolk & Western Railway Co. v. North Carolina*, supra, 297 U.S. 688, this Court stated:

> "A finding that the statute, though fair upon its face, is oppressive toward the railway in its practical operation cannot rest upon so fragmentary and partial a showing of facts. We must bear in mind steadily that the burden is on the taxpayer to make oppression manifest by clear and cogent evidence."

There is no "clear and cogent evidence" in this case that the Iowa sales formula visits upon Moorman violations of its constitutional rights as alleged by producing extraterritorial taxation, multiple taxation, or discrimination. Such a showing cannot be made, as a matter of constitutional law, by limiting the inquiry to a comparision of the apportionment percentages of the Iowa sales formula and Illinois three factor formula in the abstract, ignoring Moorman's income-producing activities in all states whereas it is the overall net income derived therefrom which is subject to apportionment and not merely gross income less deductions pinpointed to Iowa and Illinois, failing to consider or point out the profitability of Moorman's operations in all states, failing to point out the precise jurisdictional sources of Moorman's income in all states, failing to consider Moorman's tax bases computed for all states, assuming that an apportionment formula must contain geographical calculations of capital and labor, assuming Moorman was taxed by the Iowa formula on

100% of its income derived from Iowa sales when it was not, and speculating by hypotheticals that the Iowa sales formula gives direct commercial advantages to Iowa-based companies and penalizes imports of foreign corporations. Such is Moorman's constitutional attack both from the standpoint of the facial validity of the Iowa formula and validity as applied to Moorman's net income. Clearly, that attack is defective.

V. Reversal Of The Decision Of The Iowa Supreme Court Would Create A Constitutional Formulary Contrary To The Respect Shown By This Court Toward State Taxation.

This Court, historically, has refrained from requiring the states to pursue any specific apportionment formula. Moreover, "there is nothing in the constitution which requires a state to adopt the best possible system of taxation." *New York v. Latrobe*, 279 U.S. 421 (1929). The Supreme Court of Colorado aptly stated in *General Motors Corp. v. Colorado*, 181 Colo. 360, 367, 509 P.2d 1260, 64 (1973):

> "It was not the trial court's function, nor ours here, to decide which formula was the more economically sound. This is a policy decision for the legislature."

In analyzing the opinions of this Court in apportionment cases, the Iowa Supreme Court stated:

> "As noted, in its opinions in this area the Supreme Court has recognized: (1) the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as the unitary business under consideration here; (2) rough approximation rather than mathematical precision is sufficient; (3) the heavy burden cast upon the taxpayer in challenging a legislative enactment on constitutional grounds; and (4) the utmost leeway must be given the states both in their choice and application of formulae in this connection as long as basic considerations of due process and equal protection are observed." (A. 130)

The above constitutional principles expounded and painstakingly formulated by this Court over many years would be jettisoned if the Iowa Supreme Court's decision is reversed in this case. Moorman really wants this Court to imprint the equally weighted three factor formula as the exclusive one in the Constitution (Moorman Brief, pp. 37-40). In essence, according to Moorman and its economist allies, no other formula is economically sound and the taxing power of the states should be imprisoned within the three factor formula provided in the Uniform Act. This Court has never made such an imposition upon the states in pursuing their fiscal policies and has consistently sustained diverse apportionment formulae. Such decisions by this Court in those cases have not created a detriment to free trade among the states and there is nothing to suggest that the affirmance of the decision of the Iowa Supreme Court in the present case would be detrimental as alleged. The argument that such a detriment would exist many be appropriate for congress to consider as a matter of wisdom of state income tax laws affecting interstate commerce, but it should be rejected in this judicial forum.

CONCLUSION

The decision of the Iowa Supreme Court that the Iowa single sales factor apportionment formula is facially constitutional and constitutional as applied to the net income of Moorman is based upon the constitutional principles so carefully and painstakingly formulated by this Court in a number of cases. To reverse that decision and find either that the Iowa formula is facially invalid or invalid as applied to Moorman would create a constitutional formulary and allow a taxpayer to strike down any formula on the basis of mere assumptions and hypotheticals.

On its face, the Iowa statutory sales formula does not cause extraterritorial taxation, but reasonably apportions net

income to Iowa in conformance with the guarantees of due process.

On its face, the Iowa statutory sales formula does not create multiple taxation and discrimination against interstate commerce in violation of the commerce clause.

On its face, the Iowa statutory sales formula does not violate equal protection, but treats all corporations doing business in Iowa and engaged in selling goods in the Iowa market place alike.

As applied to Moorman's net income, the stipulated record herein does not show that the Iowa formula transgresses any of Moorman's constitutional rights.

In view of the appropriate constitutional principles to be applied in resolution of the instant tax dispute, the viability of the Iowa sales formula cannot be seriously challenged as a constitutional disruption of the United States common market.

The decision of the Iowa Supreme Court should be affirmed and Moorman's appeal dismissed.

Respectfully submitted,

Richard C. Turner
Attorney General of Iowa

Harry M. Griger
Assistant Attorney General
Lucas State Office Building
Des Moines, Iowa 50319

Attorneys for Appellee

APPENDIX

APPENDIX A

CONSTITUTION OF THE UNITED STATES

ARTICLE I.

* * *

Section 8. The Congress shall have Power . . .

* * *

To regulate Commerce . . . among the several States . . . ;

AMENDMENT 14.

Section 1. * * *; nor shall any State deprive any person of . . . property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX B

CODE OF IOWA

422.33 Corporate tax imposed

A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount . . .

1. If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the trade or business within the state, said net income

attributable to the state to be determined as follows:

a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside of the state.

b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

* * *

Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

The gross sales of the corporation within the state shall be taken to be the gross sales from goods delivered within the state, excluding deliveries for transportation out of the state.

For the purpose of this section, the word "sale" shall include exchange, and the word "manufacture" shall include the extraction and recovery of natural resources and all processes of fabricating and curing. The words "tangible personal property" shall be taken to mean corporeal personal property, such as machinery, tools, implements, goods, wares, and merchandise, and shall not be taken to mean money deposits in banks, shares of stock, bonds, notes, credits, or evidence of an interest in property and evidences of debt.

2. If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the director and applied to his business, has operated or will so

operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the director a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances with such detail and proof and within such time as the director may reasonably prescribe; and if the director shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequitable, the director shall redetermine the taxable income by such other method of allocation and apportionment as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state; not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment.

422.35 Net income of corporation -- how computed.

The term "net income" means the taxable income less the net operating loss deduction, both as properly computed for federal income tax purposes under the Internal Revenue Code of 1954, with the following adjustments:

1. Substract interest and dividends from federal securities.

2. Add interest and dividends from foreign securities and from securities of state and other political subdivisions exempt from federal income tax under the Internal Revenue Code of 1954.

3. Where the net income includes capital gains or losses, or gains or losses from property other than capital assets, and such gains or losses have been determined by using a basis established prior to January 1, 1934, an adjustment may be made, under rules and regulations prescribed by the director, to reflect the difference resulting from the use of a basis of cost or January 1, 1934, fair market value, less depreciation allowed or allowable,

whichever is higher. Provided that the basis shall be fair market value as of January 1, 1955, less depreciation allowed or allowable in the case of property acquired prior to that date if use of a prior basis is declared to be invalid.

4. Subtract fifty percent of the federal income taxes paid or accrued, as the case may be, during the tax year, adjusted by any federal income tax refunds; and add the Iowa income tax deducted in computing said taxable income.

5. Add the amount by which the basis of qualified depreciable property is required to be increased for depreciation purposes under the Internal Revenue Code Admendments Act of 1964 to the extent that such amount equals the net amount of the special deduction allowed on the basis of the amount by which the depreciable basis of such qualified property was required to be reduced for depreciation purposes under the Internal Revenue Code Amendments Act of 1962. The "net amount of the special deduction" shall be computed by taking the sum of the amounts by which the basis of qualified property was required to be decreased for depreciation purposes for the years 1962 and 1963 and subtracting from it the sum of the amounts by which the basis of such property was required to be increased, prior to 1964, for depreciation or disposition purposes under the Internal Revenue Code Amendments Act of 1962.

Provided, however, that a corporation affected by the allocation provisions of section 422.33 shall be permitted to deduct only such portion of the deductions for net operating loss and federal income taxes as is fairly and equitably allocable to Iowa, under rules prescribed by the director.

CERTIFICATE OF SERVICE

I, Harry M. Griger, certify that I served printed copies of the foregoing Brief For The Appellee on the 23rd day of January, 1978, by depositing the same in the United States mails, with first class postage prepaid, addressed to the following named persons at the addresses shown:

40 copies to:

Hon. Michael Rodak, Jr.
Clerk, Supreme Court
of the United States
Supreme Court Building
No. 1 First Street, N.E.
Washington, D. C. 20543

3 copies to:

Donald K. Barnes
26 Palm Club
Pompano Beach, Florida 33062
Counsel for Appellant

3 copies to:

Walter R. Brown
John V. Donnelly
1200 Register & Tribune Building
Des Moines, Iowa 50309
Counsel for Appellant

Harry M. Griger
Assistant Attorney General
Lucas State Office Building
Des Moines, Iowa 50319
Counsel for Appellee